P.O. Box 2600
Valley Forge, PA 19482-2600

(610) 669-1000
www.vanguard.com

August 12, 2014

Financial Stability Board
Foreign Exchange Benefits Group
c/o FSB@bis.org

Re: Foreign Exchange Benchmarks Consultative Document

Dear Sir or Madam,

Vanguard[1] appreciates the opportunity to provide the Financial Stability Board's Foreign Exchange Benchmark Group (the "**FSB**") with our views on the proposals in the FSB's Foreign Exchange Benchmarks Consultative Document (the "**Consultative Document**") concerning the integrity of foreign exchange ("**FX**") benchmarks and the potential for certain practices to afford opportunities for manipulation of the benchmark fixings.[2]

As a part of the prudent management of our mutual funds and other portfolios, we enter into FX transactions and derivatives to achieve a number of benefits for our investors including hedging portfolio risk, lowering transaction costs, and achieving more favorable execution compared to traditional investments.

The integrity of benchmarks generally, and FX benchmark fixings specifically, is fundamental to the asset management community, both with respect to passive index funds which strive to replicate the performance of targeted benchmarks and with respect to the hedging of FX risk. In particular, the WM/Reuters ("**WMR**") 4pm London fix (the "**WMR fix**") allows for the efficient aggregation of orders and expands netting opportunities in managing FX risk. Vanguard agrees that asset managers need to rely upon credible, transparent and robust benchmarks and foreign exchange benchmarks in particular.

We commend the FSB for its efforts to assess concerns related to practices involving FX benchmark fixings and in seeking public comment on proposed recommendations to address potential manipulative behavior. Vanguard is sensitive to the potential for possible market manipulation linked to the structure of trading around the benchmark fixings and is supportive of

[1] Vanguard offers more than 170 U.S. mutual funds with total assets of more than $2 trillion. We serve approximately 9 million shareholder accounts. Worldwide, Vanguard manages more than 150 index tracker funds, ETF's, and separately managed accounts, with aggregate assets of more than US$ 1.6 trillion. These vehicles seek to track the performance of equity indices sponsored by FTSE, MSCI, S&P, Russell, Mergent, and fixed income indices sponsored by Barclays and UBS. Vanguard also manages more than 65 actively managed funds, with assets of more than US$ 700 billion; these funds use various indices as benchmarks to help investors compare a fund's performance to the performance of a particular market or market sector as measured by an index. (All data is as of 31 January 2013.)

[2] Vanguard is a strong supporter of global reforms to the derivatives markets to bring much-needed transparency and regulation including subjecting derivatives to regulatory oversight, requiring the clearing of standardized swaps, and mandating consistent margin practices with respect to non-cleared swaps.

the FSB's proposed remedies to address these structural issues as well as to examine whether there is a need and scope to improve the construction of the benchmarks themselves. We agree with the FSB analysis on the necessary improvements as to the calculation methods and data input from a broader range of sources, as well as on the need for a central trading utility.

Vanguard appreciates the opportunity to provide feedback on several of the recommendations.

1. The group recommends the fixing window be widened from its current width of one minute. It seeks feedback from market participants as to the appropriate width of the calculation window.

While we think an auction or some type of natural crossing mechanism on a consolidated trading venue, much like an equity or swaps trading exchange, is the optimal solution, we view the widening of the fixing window as an appropriate measure to address the potential for market manipulation prior to, or concurrent with, the rate fixing.

We believe that the appropriate width of the calculation window should be no less than 2 minutes and no more than 5 minutes for most major liquid currency pairs. It would also be appropriate for the width of the calculation window to vary based on the relative liquidity of the currency pairs with less liquid pairs afforded a slightly longer calculation window. Note that it is important that any changes to the WMR fix mechanism should also be made consistently with other fixing points throughout the day.

While we recognize that the current calculation window of one minute may allow for price volatility, and may present an opportunity for manipulation by dealers trading ahead of the fixing, too long of a calculation window could introduce adverse market consequences.

If the calculation window is too long, the potential for increased volatility may lead dealers to be less willing to provide efficient pricing at the fixing mid given the increased challenge for them to hedge their risk. The greater the spread between the dealer pricing and the fixing mid would create significant challenges to asset managers in their efforts to both invest in replication of a benchmark index and to hedge at or near the fixing rate. These challenges could serve to increase the tracking error of index-linked portfolios to the detriment of fund shareholders.

Also if the calculation window is too wide, dealers would not have a clear assessment of the aggregate size of their customers' FX orders at the opening of the calculation window as additional orders could be made after the window opening. FX orders from asset managers are based on a number of inputs including shareholder subscriptions and redemptions and security purchases and sales. As these inputs are fluid, the order size is ideally set at or just prior to the actual fixing and may not be complete at the opening of an overly widened calculation window. Again, this would introduce considerable challenges – both with respect to the calculation itself and with respect to dealers pricing orders received after the window opening. The potential for post-opening orders would naturally increase the spread between dealer pricing and the fixing mid and, as noted above, increase the tracking error for the passive index funds.

2. The group seeks feedback from market participants as to whether there is a need for alternative benchmark calculations (such as a volume weighted or time weighted benchmark price) calculated over longer time periods of up to and including 24 hours.

As noted in our above response to the first recommendation, although it is advisable and beneficial to reasonably extend the time period of the calculation window to address the potential for manipulation, we believe extending the window over too long a period of time would have a detrimental impact on the market.

It is extremely important to asset managers that any benchmark solution is achievable, tradable and trackable. As noted above, introducing a significantly longer time period for the calculation window could serve to compromise the tradability of the benchmark fix and thereby heighten tracking error risk for index funds.

Assuming that the calculation window is reasonably widened as noted above, with respect to a volume weighted benchmark, we agree the WMR should evaluate and monitor the venues it uses to calculate the fixing rates. It would be preferable for WMR to obtain real volumes traded at such exchanges during the pricing window in order to calculate a volume weighted average price. As current calculations do not account for the volume executed at a price, the potential for price manipulation is increased.

3. The group also seeks feedback from market participants as to whether the fixing windows should continue to be centered exactly on the hour (half hour) or whether the fixing window should close or start on the hour. Market participants should consider whether this view changes depending on the size of the window.

We would not recommend moving the calculation methodology from fixing on the hour. We are still in favor of the hour being the center point of the calculation, starting before the hour and ending after the hour. The existing approach of centering the fixing on the hour is also consistent with our position that while the calculation window should widen, it should widen to no more than 5 minutes for liquid currency pairs and possibly slightly longer for less liquid pairs.

6. The group supports the development of industry-led initiatives to create independent netting and execution facilities. However, it also is interested in seeking feedback from market participants on the development of a global/central utility for order-matching to facilitate fixing orders from any market participants.

As noted above, an auction or some type of natural crossing mechanism on a consolidated trading venue, much like an equity or swaps trading exchange, is the optimal solution. Such an approach is most likely to generate natural price discovery. Such a venue could conduct a closing auction (e.g.: an auction during the final 10 minutes of the trading day) and the price derived therefrom would eliminate the potential manipulation presented by the current WMR fix. Through conducting an auction at the market close, a market clearing rate would be achieved.

Ideally, asset managers such as Vanguard would have direct access to such a trading venue and would not be reliant on bank / dealer access. This would provide market participants with full transparency of flows and imbalances into the closing auction with the ability to utilize limit orders within this clearing rate.

In addition, such a trading venue would support "Market on close" and "Limit on close" order types. Closing imbalances would be fully displayed with the ability for traders to offset these imbalances. We fully support a thoughtful migration from a bank / dealer-driven over-the-counter market to a regulated consolidated trading venue, much like an equity or swaps trading exchange.

15. The group recommends that asset managers, including those passively tracking an index, should conduct appropriate due diligence around their foreign exchange execution and be able to demonstrate that to their own clients if requested. Asset managers should also reflect the importance of selecting a reference rate that is consistent with the relevant use of that rate as they conduct such due diligence.

Asset managers have important due diligence responsibilities concerning the use of financial benchmarks flowing from both regulatory requirements and industry best practices.

As confirmed to shareholders in fund disclosure, transaction cost analysis is rigorously performed to meet such requirements and best practices.

Vanguard supports the FSB's efforts to increase the overall transparency of FX benchmark fixings and thereby address the potential manipulation for the benefit of market participants including fund shareholders.

* * *

In closing, we thank the FSB for the opportunity to comment on the recommendations proposed in the Consultative Document and appreciate the FSB's consideration of Vanguard's views. If you have any questions about Vanguard's comments or would like additional information, please contact William Thum, Principal, at (610) 503-9823 or Jane Wagner, Senior Counsel at (610) 669-3674.

Sincerely,

/s/ Tim Buckley

Managing Director
and Chief Investment Officer
Vanguard

/s/ Andrew Maack

Principal
and Global Head of Foreign Exchange Trading
Vanguard